

BUDGET BRIEF

NEWS ON CALIFORNIA STATE BUDGET ISSUES FROM THE SENATE COMMITTEE ON BUDGET AND FISCAL REVIEW

2006 – Number 1

Message from the Chairman

This “Budget Brief” is intended to provide you with a better understanding of California’s State Budget and the many program areas it encompasses. From time to time, a “Budget Brief” will be issued covering topics related to the budget. We hope you find it useful.

Status of Current Year (2005-06) Budget

On July 7, 2005, the Legislature passed SB 77, the 2005 Budget Act (Chapter 38, Statutes of 2005) and companion legislation, SB 80 (Chapter 39, Statutes of 2005), that revised various items to the main budget. In enacting these bills, the Legislature met its Constitutional obligation to pass a balanced budget. The table below broadly summarizes the State General Fund for fiscal years 2004-05 and 2005-06.

GENERAL FUND SUMMARY (dollars in millions)

	Final 2004 Budget (revised)	Final 2005-06 Budget
	2004-05	2005-06
Prior-Year Balance	\$ 7,279	\$ 7,498
Revenues and Transfers	79,935	84,471
Economic Recovery Bonds	2,012	—
Total Resources Available	89,226	91,969
Expenditures	81,728	90,026
Fund Balance	7,498	1,943
Reserves:		
Liquidation of Encumbrances	-641	-641
Economic Uncertainties	\$ 6,857	\$ 1,302

Broad Overview of 2005 Budget Act

- The 2005 Budget Act (SB 77) provided a balanced budget as required by the State Constitution.
- Total revised General Fund resources were estimated at \$91.9 billion, while estimated expenditures are approximately \$90 billion. (The total budget for all funding sources was projected at \$117.3 billion.)
- The budget includes a General Fund reserve of \$1.3 billion.

- The budget did not include any general tax increases, but is premised on certain fee increases, particularly in the area of higher education.
- The budget, at the time of passage, did not rely on assumed unachievable savings, solutions, or federal funding.
- Additional details on specific actions taken in the 2005-06 Budget can be found in the Senate Budget Committee's *Final Action Report, a Summary of the 2005 Budget Act*.

Mid-year Budget Update

November's Special Election. In Spring 2005, the Governor called a special election that, among other things, called for substantial constitutional changes to the current budget process and mid-year budget adjustments. The measure, Proposition 76, would have created an additional spending limit, granted the governor new power to reduce state spending, altered key provisions of Proposition 98, and made a number of other changes related to transportation funding, loans between state funds, and payments to various entities. Proposition 76 was rejected by the people of the State of California.

The Legislative Analyst Office (LAO), in late November, provided updated fiscal projections for the budget year and beyond in their *California's Fiscal Outlook* publication. According to the LAO, the combined effect of changes will result in a revised year-end General Fund reserve of \$5.2 billion. According to the LAO, two key changes have occurred since adoption of the 2005 Budget Act.

1. The first, revenues are up – approximately \$3.8 billion (current-year and prior-years combined) more than anticipated when the Budget was enacted. Most of the additional revenue is due to stronger personal income tax, but also gains in corporate tax.
2. Second, overall expenditures are down slightly – by approximately \$80 million.

The LAO indicates their forecast is not a prediction, but rather a reasonable “baseline” projection – a starting point for legislative deliberations. Consistent with this viewpoint, there are a few things to keep in mind about the current and prospective budgets:

1. Since the release of the LAO report, a California Superior Court ruled the sale of pension obligation bonds (POBs) violates provisions of the state constitution related to issuance of debt. The 2005 Budget anticipated the issuance of POBs to achieve \$525 million in General Fund savings for the Public Employees' Retirement System (PERS).
2. The LAO assumes Proposition 98 funding in 2006-07 will be at the minimum guarantee level. However, this is \$731 million less than the amount needed to fully fund enrollment and cost-of-living adjustments (COLAs) for K-14 education programs.
3. There is no estimate of additional federal funds, which may offset some General Fund expenditures in 2006-07. In addition, the LAO analysis did not quantify policy changes that the federal government is currently contemplating that might affect the budget.

LAO indicates “while the improved near-term and long-term outlooks are clearly positive news, the state is still not out of the woods with respect to its longer term structural deficit problem.” The Legislature now awaits the presentation of the Governor's proposed 2006-07 Budget. The proposed budget is expected to be released on January 10, 2006.

Primer on the California State Budget Process and Timeline

Legislative review of the proposed Governor's Budget begins in early January and typically runs through late June. The State Constitution requires the Governor to submit a balanced budget proposal to the Legislature by January 10 of each year. The proposal details the Governor's spending plan for the fiscal year beginning July 1. (The fiscal year runs from July 1 through June 30.) Below is a brief description of the budget process.

- Preparation of the Governor's Budget (July – September). Budget instructions are issued by the Department of Finance (DOF) – acting on behalf of the Governor – to all departments. The instructions are used by the departments in preparing their budgets for submission to DOF. DOF analyzes the departmental proposals, and, in addition, may initiate its own proposals.
- Review and Approval (October – December). After the proposals are analyzed, DOF conducts meetings with each agency. The DOF then sends the departmental proposals, along with its own recommendations, to the Governor for his review and approval. When all decisions are made, the proposed budget is then sent to the Legislature.
- Budget Bill Introduction (January). With the submission of the Governor's Budget on January 10, the Chairpersons of the Senate Budget and Fiscal Review and Assembly Budget Committees each introduce a Budget Bill that contains appropriations to finance the program levels proposed in the Governor's Budget. This in no way obligates the Chairpersons to support the Governor's proposals. The Budget Bill goes to the full Budget Committee in each house and then is referred to specialized budget subcommittees for hearings.
- Legislative Hearings (February – May). The full committee of each House typically meets in January or early February to begin the hearing process. Generally, the Director of Finance is given an opportunity to present the Governor's proposed budget to the full committee. The full committee hearings provide a forum for legislative questioning that will eventually segue into more specific subcommittee hearings.

In addition, the full committee and subcommittees may conduct oversight hearings during February in order to review departmental and/or program compliance with legislative policy and fiscal direction.

Budget subcommittees will conduct more detailed hearings throughout the Spring on the Governor's Budget and consider DOF amendment letters (usually issued in April and the May Revision), Legislative Analyst Office (LAO) budget recommendations, and other issues raised by Legislators, various constituent groups, and the general public.

In mid-May, the Governor provides an update to his/her January revenue forecast and makes caseload adjustments. If the forecast changes significantly, the Governor may also propose changes in spending at this time. The update is known as the "May Revision." The subcommittees have about one week to consider and act on the May Revision. At the end of May, the full budget committees in each House of the Legislature may hold additional hearings prior to convening a Budget Conference Committee. The budget bills in both houses are also amended to reflect actions taken by the subcommittees and full budget committees.

- Budget Conference Committee Resolves Differences (June). Once both Houses have finalized their versions of the budget, a conference committee of members from both Houses is formed to (1) work out differences between the two proposed versions of the budget and (2) incorporate a “conference committee report” into one measure. There is no public testimony heard during the conference committee hearings.
- Possible Leadership Meetings (June/July). In recent years, some budget differences have been worked out in meetings, known as Big 5 meetings, of the Governor, Senate President pro Tempore, Assembly Speaker, Senate Minority Leader and Assembly Minority Leader.
- Final Legislative Approval (June/July). The conference committee report is then sent back to the floor of each House for final approval.
- Governor’s Action (June/July). The Budget Bill approved by both houses is sent to the Governor. The Governor can exercise his/her veto discretion (blue pencil), which permits reducing or eliminating the entire amount of a particular appropriation. The Governor then signs the Budget Bill and it becomes the Budget Act. The Legislature may then consider overriding any vetoes the Governor has made and may do so by a two-thirds vote of each House.